Defined Benefit Plan Update

Male voice:

[Slide 1] Good day, ladies and gentlemen, and welcome.

All lines have been placed in a listen-only mode.

If you should require assistance during the conference, please press star zero to reach a live operator. At this time, it is my pleasure to turn the floor over to your host, Angel Carrington.

Angel, the floor is yours.

Ms. Carrington:

Thank you. Good afternoon; as he indicated, I am Angel Carrington, the Acting Director of IRS Employee Plans Customer Education and Outreach. Thank you for joining us today and welcome to our Defined Plan Benefit Update Webinar.

[Slide 2] Today we'll be hearing from Carol Zimmerman and Jeff Milling. They are actuaries in the office of Employee Plans. Jeff is sitting in today is place of Larry Heberle who was unable to join us during this session.

Now, before we get started, I would like to point out a few things. We'll email a certification of completion to everyone registered for today's forum if you attend at least 50 minutes of the presentation. Enrolled agents, retirement plan agents, and actuaries can receive continuing education credit for this session. Other tax professionals should consult their licensing organization to see if today's session qualifies for continuing education credit.

As with all our presentations, the comments expressed by our speakers should not be construed as IRS formal guidance. Although we will not be addressing questions submitted during today's webinar, you're welcome to use the "Ask Questions" feature of the program to provide your comments and concerns regarding the guidance being discussed this afternoon. Although we may not be able to answer all the questions individually, we will address the trends in the questions and answer sheet that will be posted with the recording of this program at a future date.

[Slide 3] Now, here at the IRS we have many retirement plan resources that are available to you. If you'll take a look at slide three, we'll see our retirement plan Web page. You can also get there by going to the main IRS.gov landing page where you click on the "Information For" drop-down box on the upper right-hand side of the screen and select "Retirement Plans."

[Slide 4] On slide four, we'll see a graphic of how you can subscribe to our free electronic newsletters. To subscribe, select "Newsletters" in the left navigation bar, choose "Subscribe" and then select "Retirement News for Employers" - that is our newsletters for employers sponsoring retirement plans - and "Employee Plans News - that is our newsletter for retirement plan professionals.

And with that, thank you; I'm going to hand it over to Carol and Jeff.

Carol Zimmerman:

[Slide 5] Thank you, Angel. So when we initially scheduled this webinar, I did not have the -- I did not realize I would have the privilege of talking about guidance on HATFA that was issued last Thursday in Notice 2014-53. And I certainly didn't expect that I would have the opportunity to discuss the hybrid plan regulations which were released just this morning. So although the description of this session promised a discussion of recent and pending guidance, I thought you have might find it more helpful if I spent my time discussing the guidance that has been released in the past week.

The PowerPoint slides that were posted online reflect the remarks I'd intended to make prior to this morning, so you can use the slides to glean some of the information described in the webinar announcement, even though we will not be discussing this other guidance today.

So let me start with a quick description of the hybrid plan regulations. This morning we released regulations that finalized the proposed hybrid plan regulations issued in October 2010 and a new set of proposed regulations dealing with transition rules for implementing the market rates of return included in the final regulations.

The final regulations answer a number of important questions for hybrid plans, including the final market rates of return. These regulations retain the proposed rule that the market rates of return contained in the regulations constitute the exclusive list. No interest rates would meet the market rate of return rules if they are not described in the regulations.

However, the regulations authorize the IRS and Treasury to issue supplemental guidance adding new permissible rates or increasing the rates currently provided in the regulation if changes are warranted.

The final regulations also modify the proposed market rates of return in response to comments – so, for instance, the maximum fixed interest rate is increased from the proposed rate of five percent and will now be six percent. Segment rates can be used either with or without the MAP-21 and HATFA adjustments. The maximum fixed rate permitted in combination with government bond based rates, which are essentially the rates that were permitted under Notice 96-8, increased from four percent to five percent.

However, the maximum guaranteed fixed rate that can be used in combination with corporate bond based rates, such as the segment rates, retain the maximum guaranteed rate of four percent that was in the proposed regulations.

Now, plans are now permitted to use -- or under these regulations would be permitted to use -- the actual rate of return on a subset of plan assets rather than the total plan assets as proposed, as long as the subset meets certain conditions.

Now, the proposed regulations that were also issued this morning provide guidance on changing interest rates to meet the final market rate of return rules. Now, generally a plan cannot be amended to reduce future interest credits on the account balance that's already accrued as of the date of the amendment without violating Section 411(d)(6).

However, the proposed regulations provide limited relief from Section 411(d)(6) if a plan's interest crediting rate doesn't comply with the market rate of return restrictions, as long as that rate is reduced prospectively only, and only to the extent required to meet the new rules.

So, for example, if the plan uses a fixed interest crediting rate higher than the permitted rate of six percent, the plan must be amended to reduce the rate to six percent but no lower. The proposed regulations also provide guidance as to how to adjust the interest rate if it is based on the combination of rates. So, for instance, if a plan uses an interest crediting rate that is the greater of a variable rate or a fixed rate that is higher than permitted, the plan can be amended to either reduce the fixed rate to four or five percent, as applicable, and retain the variable rate, or it can eliminate the variable rate and use a fixed rate of six percent, even if the fixed rate was lower than six percent.

Let's see. The proposed regulations also address other types of rates. Excuse me one second.

The final regulations are generally effective for plan years beginning on or after January 1, 2016.

The proposed rules apply to amendments adopted on or after the final transition regulations appear in the Federal Register, but they can be applied to earlier amendments. We encourage you to read these regulations and submit your comments. Please see the preamble of the regulations for details on how to submit those comments.

And so, now, as they say, we return to what we originally planned to do, and so I am moving on to slide six of your presentation.

[Slide 6] I wanted to talk a little bit about HATFA, which was enacted on August 8, and provides funding relief that is very similar to MAP-21 except for the timing. So whereas plans were not required to use MAP-21 until the plan year after it was enacted, HATFA is retroactively effective to 2013 with an option to defer its effect to 2014. Therefore, HATFA potentially affected contributions due only a little over a month after its enactment.

Now, a plan sponsor has the option to defer the application of HATFA to 2014 for all purposes or just for purposes of applying the Section 436 benefit restrictions. Therefore, a plan sponsor can take advantage of the funding relief for 2013 without having to change the plan's operations under Section 436.

[Slide 7] In looking at slide seven, the key provision of HATFA is the extension of the MAP-21 interest rate corridors as shown on this table.

[Slide 8] Now, HATFA includes additional provisions as well as the interest rate corridors.

It provides that the MAP-21 and HATFA rates cannot be used for applying the Section 436 restrictions on accelerated benefits, including lump sums, if the plan sponsor is in bankruptcy. This rule applies for distributions with annuity starting dates in plan years beginning after December 31, 2014,

HATFA also extends the requirement to report the effect of using the HATFA rates in the annual report to participants, corresponding to the extension of the interest rate corridors, and it also includes a technical correction on the alignment of segment rates for plans with valuation dates other than the first day of the plan year. Essentially, these would be end-of-year valuations.

[Slide 9] IRS and Treasury issued guidance on HATFA in Notice 2014-53. Notice 2012-61, which provided guidance on MAP-21, remains in effect, except where the rules were changed by HATFA.

[Slide 10] Using the HATFA rates for 2013 is the default. An election must be made to defer the rates to 2014 under the terms of the Act. However, to avoid situations in which a plan sponsor inadvertently defaults into retroactive application of these rates, Notice 2014-53 provides for a deemed election to defer HATFA to 2014 for all purposes if the 2013 SB is filed by December 31, 2014, using the MAP rates. So if a Schedule SB is filed at that time using MAP-21 rates, the plan sponsor will not need to take any additional action to defer the HATFA rates to 2014.

Now, alternatively, the plan sponsor can make an election to defer the HATFA rates to 2014 by making a written election, which is due by the deadline for filing the 2013 Form 5500 or December 31, 2014, if later. But note that a written election is required in any circumstance if the sponsor wishes to defer the use of the HATFA rates for Section 436 purposes only.

[Slide 11] Now, if the 2013 Schedule SB was filed using MAP-21 rates, and therefore, the deemed election to defer has occurred, the plan sponsor can revoke that deemed election. This can be done in one of two ways.

First, the sponsor could file an amended Form 5500 with a 2013 Schedule SB reflecting the HATFA rates by December 31, 2014.

Or, if the sponsor does not have enough time to obtain a revised Schedule SB by December 31st, the sponsor can make a written election by that date and then follow up with a revised 2013 Form 5500 and Schedule SB by the time the 2014 Form 5500 is timely filed. However, this second option is not valid unless a copy of the written election that is done by December 31st is also emailed to the PBGC by that date, and this option, the second option, is not available if the plan sponsor is in bankruptcy at the time of the election.

[Slide 12] Note that in any event, the Schedule SB for a plan year must reflect the HATFA rates if they are used for that plan year.

We are aware that a number of 2014 valuations were completed using the MAP-21 rates prior to the enactment of HATFA, but we did not see any statutory authority for waiving the use of HATFA rates for the 2014 plan year. And also, when you're reflecting these rates, please don't forget that the new rates affect not only the funding target and target normal costs, but other calculations as well, including the discounted contributions receivable that are included in the value of assets. Those would have to be discounted based on the new HATFA rates.

[Slide 13] Now, similar to Notice 2012-61, the HATFA notice allows plan sponsors to reverse certain elections and to recharacterize contributions that were made on the MAP-21 rates but which are no longer needed when the HATFA rates are used.

[Slide 14] These changes are generally available for elections and contributions that are made on or before September 30, 2014, with the elections to reverse or recharacterize due by December 31, 2014.

However, these changes do not apply to elections made in connection with presumed AFTAPs, with one exception which we will discuss in a minute. And these changes cannot be made if the change would result in an unpaid minimum required contribution for any plan year prior to 2014 or if they would trigger a 436 restriction that would not otherwise apply.

Now, because we are somewhat short on time today, this is a very broad description, so please refer to the notice for further details and requirements; I did not cover all the requirements in this description.

[Slide 15] Moving on to slide 15. The effect of HATFA rates on Section 436 restrictions is very similar to the implementation of MAP-21 rates under Notice 2012-61. If HATFA rates are deferred to 2014 for 436 purposes after the AFTAP was certified using the MAP-21 rates, any resulting change in plan operations is implemented prospectively only unless the sponsor elects to apply the change retroactively -- and if it is applied retroactively, it would be applied back to the date of the original 2014 AFTAP certification. It would not affect the presumption period.

However, and this is the exception I alluded to earlier, if the 436 restrictions were applied using the HATFA rates for the 2013 plan year, then the 2014 benefit restrictions must be applied consistently. So, therefore, in that situation, the 2014 presumed AFTAP is based on the 2013 HATFA AFTAP that was certified for that year. So, accordingly, elections or deemed elections to reduce the funding balances and 436 contributions made in connection with the original MAP-21 presumed AFTAP for 2014 can be reversed, despite the general rule requiring that these changes be made only in connection with certified AFTAPs. But, of course, if you are reversing any elections or recharacterizing contributions based on the 2014 presumption in that situation, you would be using the presumed AFTAP based on the 2013 HATFA AFTAP.

Note that if the HATFA changes are applied prospectively, the new AFTAP must be certified by December 31, 2014. However, in response to one of the questions that we received, if using the HATFA rates does not result in a material change in the AFTAP (that is, it doesn't result in a change in operations either for the current year or during the presumption period for the following year), then no recertification is necessary.

Notice 2014-53 also provides simplified correction methods for affected distributions and these are very similar to those in Notice 2012-61.

[Slide 16] We have received a number of questions regarding the lack of a specific provision for reversing an election to use a funding balance to offset the minimum required contribution. Now, we did not specifically provide for this in Notice 2014-53 because we believe that the existing regulations, along with some of the relief in 2014-53, provide the relief that plan sponsors are requesting.

So although for many plans the deadline for revoking excess “use” elections under Section 1.430(f)-1 is past, the regulations provide that any unrevoked excess “use” election becomes an election to reduce the funding balance. And that funding balance, that election to reduce the funding balance, can then be reversed under Notice 2014-53.

On the other hand, if the plan sponsor elected to use the funding balance to offset minimum required contributions and then made excess contributions, Notice 2014-53 permits late elections to credit excess contributions to the prefunding balance to replenish the amount that was used. And if a standing election was in place, the “use” election is automatically adjusted for the change in funding requirements when HATFA rates are used. So, therefore, regardless of how that “use” election came about and how it was used, we feel that there are opportunities to recapture that amount if the plan sponsor so desires.

[Slide 17] There have also been a number of questions regarding the technical correction to realign the segment rates based on the valuation date instead of the first day of the plan year as originally provided in PPA ‘06.

Based on a comment in the preamble to the final 430 regs saying that the IRS and Treasury believed that it was more appropriate to base the segment rates on the valuation date, and the fact that we reserved that paragraph in the regulations, many practitioners felt comfortable using that approach for year-end valuations. However, a number of people have been concerned that this was somehow linked to the decision as to when to reflect the HATFA rates, and they were concerned that if they deferred the HATFA rates to the 2014 plan year for all purposes, that they might lose the ability to use the technical correction for the 2013 plan year.

However, we do not read the provision in HATFA this way. We believe that if HATFA is not applied for the 2013 plan year, then the previous rules apply, which means that if the plan's actuary was comfortable aligning the segment rates based on the valuation date prior to the enactment of HATFA, he or she should continue to feel comfortable taking the same approach for 2013, whether or not the HATFA rates are applied for that plan.

Now, although not shown on the slide, I would like to address two more questions we received before I pass this over to Jeff.

We have been asked whether HATFA applies to plans that terminated prior to its enactment. We didn't include guidance in the interest of time, but I can't imagine anyone would challenge you if you used MAP-21 rates for a plan that terminated before August 8th.

We have also been asked whether elections made during the presumption period can be reversed if they were not made for Section 436 purposes. And in looking at this, we will not be asking people to state why the elections were originally made. Reversals of these elections are permitted, even if they occurred during the presumption period, as long as the plan still complies with Section 436 after those elections are reversed, taking into account the appropriate presumed and certified AFTAPs for all periods.

Now, as I mentioned earlier, we will not have time to discuss the remaining slides in my portion of the presentation because we wanted to make more time to cover the new guidance, so I will pass the microphone to Jeff at this point, but if we have time at the end of this session, we may come back and revisit some of those slides that we just skipped. Jeff.

Jeff Milling:

[Slide 29] Thank you. Carol has provided you with a great update as to what is new and exciting. I will be discussing problems encountered with dealing with prior legislation and guidance. Not as new and exciting, but it certainly is important to be aware of some of the pitfalls. I plan on reviewing many of the issues that we are encountering on examinations, but before I get into the details, I would like to provide a bit of background. This slide, slide 29, provides a nice overview of the examination process and what you might expect should you be lucky enough to participate in an EP examination. As consultants and advisors to your clients, you can provide crucial assistance in keeping the examination on track and keeping it running smoothly.

The key to an efficient examination is the sharing of information between both the examination agent and your client. Understanding what is being asked and understanding what is being provided can go a long way in moving the examination along.

[Slide 30] Depending on the technical nature of the issues involved, the examination agent may bring in an IRS specialist to assist with the exam. A key benefit of bringing in a specialist is that they can converse in the language of your experts. For example, the IRS actuary and the plan's actuary can converse on a level that others may find confusing but likely not amusing. A short call or meeting with a specialist can often clear up issues or problems without time-consuming correspondence between you and the examining agent. This list is approximately in order of the most likely appearance of the specialist in your cases. The agents work very closely with the TE/GE actuaries, and I'll discuss this further on the next slide.

Our counsel attorneys are also available to discuss technical areas and help the agent understand the legal environment surrounding an issue. Our computer audit specialists, CAS, generally get involved in the very large cases in which significant amounts of data need to be analyzed or processed.

Our engineers and financial product specialists will assist when confusion arises about assets or the proper valuation of those assets.

[Slide 31] I manage the examination group of actuaries. We are often called the field actuaries, as we are situated throughout the U.S. and work very closely with the agents. Each agent has an actuary that they can seek guidance and assistance from on their case.

Our actuaries also provide training for the agents and develop examination aids for the agents to use in working their cases.

The actuaries also work with the determination agents in reviewing their plan documents and understanding the plan language. We also assist the voluntary compliance agents with their technical issues on submissions. One advantage of our role is that we work with all the various groups and hopefully can recognize gray areas that need guidance and/or coordination to assure consistency. We then bring those issues over to Carol in our policy and ruling group.

[Slide 32] The field actuaries assist on many of the cases that the agents are working. We often assist in formulating the right wording for an information document request, reviewing the information provided, and suggesting possible follow-up questions. At the request of our agents, we often attend conferences, typically by phone, to explain issues and/or resolve points of contention. And I would tell you that if you are having difficulty communicating with the agent assigned to your case, you should consider requesting the agent ask for our assistance.

[Slide 33] Now I'd like to spend a few minutes and discuss some -- obviously not all -- of the errors/issues that we are finding on the examinations. We'll start with some general issues common to most plans and move to some specific plan type errors.

Specific areas we will cover will be Pension Protection Act, PPA type issues, cash balance and some multi-employer plan issues.

[Slide 34] Before getting into the details, I would like to emphasize that many of the issues we encounter would never had arisen if everyone had a thorough understanding of the plan document. Often problems arise due to misreading of the plan or a misinterpretation of plan provisions. Keeping the plan up to date and keeping all of the various plan providers appraised of changes is vital to good plan operation, so please read the plan.

[Slide 35] So what are some of the common examinations errors? Let's start with a basic but important area.

Plans subject to Internal Revenue Code Section 412, minimum funding requirements, are failing to receive the contributions necessary to satisfy the Code section. This is an area that one would not think would be problematic and fairly basic but occurs more than you might think.

One common reason for this failure is that not all eligible employees are being included in the plan, leading to improper funding calculations, in some cases improper compensation is being included for funding purposes. Oftentimes simply contributions are not made timely or not made at all.

And in addition, participating employers responsible for the excise taxes that result are not filing the appropriate excise tax return, the Form 5330, and/or paying that excise tax.

[Slide 36] The examination agent will verify that a proper fidelity bond is in place for the plan. Plans are required to have a fidelity bond equal to at least ten percent of the most current handled assets.

This is a DOL regulation. The maximum bond required is $500,000; however, effective for plan years beginning after 12/31/2007, the fidelity bond maximum is increased from $500,000 to $1 million for plans holding employer securities. Please note that no deductible is allowed in the bond and it must be in the name of the plan or trust, not the employer, or the bond must specifically state that the plan or plans by name are covered and that the general bond deductible doesn't apply per ERISA requirements.

[Slide 37] We are finding Internal Revenue Code Section 411 violations. Every plan is required to have provisions regarding how participants are vested in their benefits. Normally, the percentage a participant is vested is dependent on their credited service. If the employer and/or the union do not track a participant's service correctly, the vesting percentage could be incorrect. Errors that have been cited include erroneous cash-outs and forfeitures, the wrong vesting schedules being used and just plain calculation errors for a participant's vesting percentage.

[Slide 38] Loans can be an area of concern, but typically much more of a concern in a DC plan than DB plans, but we do run into them as a problem in DB plans also.

Loans are being made out of plans that don't provide for them.

In addition, loans are being made to people considered to be disqualified under 4975. Specific trouble areas relate to loans being made to highly compensated employees that violate one or more of the 4975(d) exemptions. Although this is not a defined benefit issue, I do want to mention it, because it comes up often in DC plans. Plans are providing hardship distributions without procedures in place to ensure that distributions indeed meet a hardship need. So that's the only DC thing I'll throw in there today. There are also 72(p) violations due to the original excessive length and/or amount of the loan exceeding either the 72(p) or what the plan requires. IRC 72(p) violations are also being found in relation to the failure to meet the level amortization requirements which require that payments be made at least quarterly.

[Slide 39] Plans are failing to meet the testing requirements in Section 410(b) due to the fact that they are not following the participation entry requirements of the plan and law which is resulting in the late entry of employees who must be included for testing purposes. Pay careful attention to the entry requirements in your plan to ensure that in operation you are satisfying the plan provisions.

[Slide 40] Errors are being made in benefit calculations, crediting service, reduction factors and general plan administration. These errors are being made when participant benefits are calculated. Some of the reasons for these mistakes have been identified as benefits in the provisions of the plan are misapplied, the applicable law is not fully understood, faulty participant data is used and/or provided, or combinations of the above. And oftentimes these changes in employee data or in demographics can result in a discrimination failure under Section 401(a)(4). One common example is the use of a compensation definition that is not defined in the plan document leading to improper benefit amounts.

[Slide 41] Examinations have revealed the presence of non or late amenders going back as far as TRA '86, GUST and EGTRRA. And one of the primary tasks of the examination agent is to ensure that the plan is up to date with all amendments and the form of the plan meets all qualification requirements.

[Slide 42] We are finding numerous issues with the required minimum distribution requirements of Internal Revenue Code 401(a)(9) not being met. 401(a)(9) establishes a mandatory date known as the required beginning date by which payments to a plan participant must start.

Basically a minimum payment must be made to the participant by this required beginning date and for each following year. A participant is not allowed to delay the distribution beyond this date, and normally the required beginning date for a participant who is not a five percent owner is the April 1st following the end of the calendar year in which the later of two events occurs, the participant reaches 70 ½ or the participant retires.

And for a participant who is a five percent owner, required beginning date is the April 1st following the end of the calendar year in which they attained age 70 ½, regardless of whether they retire by the end of that year. And we are finding the problem that plan sponsors often discover that required minimum payments have either not been paid timely or at all. The minimum distribution rules are qualification requirements, meaning they must be written into the plan. Failure to follow the minimum payment rules as written in the plan document can lead to the loss of plan's tax qualified status. If participants or beneficiaries do not receive their minimum distribution, they, not the plan, are subject to 50 percent additional tax on the underpayment.

So how do we fix this? The EPCRS revenue procedure is the latest update of the IRS' various resolution programs for correcting disqualifying defects in retirement plans and avoiding the tax consequences of plan disqualification. These programs are known collectively as the Employee Plans Compliance Resolution System. And employers may avoid disqualification of their plan by using the EPCRS to correct the failures. And we, as the actuaries that work very closely with the VC agents on a number of cases and our closing agreement program agents to resolve those 401(a)(9) issues. They're popping up quite often.

[Slide 43] Another area that we are finding problems with is Internal Revenue Code Section 417 violations. This issue deals with the specific rules affecting married participants who are approaching retirement and/or are ready to commence receiving benefits, who elect to receive their benefits in a form other than a qualified joint and survivor annuity. So problems include getting -- not getting spousal consent, the application of the QJ&S, the calculation, joint and survivor annuity adjustment when the non-spouse beneficiary is more than ten years younger than the employee, and QDROs, or Qualified Domestic Relation Orders.

The examination agent will review the plan administer is getting the spousal consents prior to distributing, say, lump sums. If it's not clear how adjustments have been made for J&S payments, the agent will often seek out the advice of the IRS actuary and we will help them with making sure that those calculations are done properly.

[Slide 44] Some other issues - common DB issues - Section 411(b)(1)(h) requires an actuarial increase for benefits delayed past normal retirement age. We're finding issues with no or inadequate suspension of benefits notices, plans are improperly determining the continued accrual and/or the actual increase for delayed retirement. Late contribution payments can lead to Section 430(j)(4) liquidity shortfall problems due to a lack of liquid assets and a resulting excise tax. Our actuaries assist with many cases that have missed, or paid their quarterly contributions late. The determination of the additional interest can be a complicated calculation and the actuaries will help the agents on those.

We are still finding plans that are partially funded with insurance that are including the full premium as an expense in the target normal cost, and life insurance cannot use, quote, you know, the split-funded approach post-PPA. And again, note, this is a small plan issue, as larger plans typically are not funded with insurance in this way.

[Slide 45] Again, read the plan. Plan operation must follow the plan terms. We discussed these issues earlier, but be aware that EP agents will sample check benefit calculations for distributions and for accrued benefits under the plan.

One area that seems to be a problem is that the 2006 final regulations on relative value disclosure are not being followed in all cases. We are seeing cases without any notices being provided, as well as cases with inadequate disclosure. We do understand that there are options for you to take in this disclosure and the agents are not looking for perfection, but rather, clear evidence that disclosure has been made.

[Slide 46] The Pension Protection Act of 2006, PPA, made significant changes to funding requirements and administrative practices for defined benefit plans, including cash balance plans. Internal Revenue Code Section 430 describes the new funding requirements under PPA. And in addition, IRC Section 401(a)(29) was added to provide that plans not in compliance with the new restrictions under IRC Section 436 may be disqualified.

So what are some of the areas that we are finding compliance problems due to PPA?

Mostly, a lot of them have to do with elections.

Elections to use or reduce the prefunding and/or carry overbalances -- these are the credit balances -- are being made late or they're not being dated and it's not possible to determine when these elections were actually made.

The elections to use the prefunding and carryover balances to meet quarterly contributions are also being made late or the elections do not specify the dollar amount to be used in those calculations.

We're also finding a number of times just late adjusted funding target attainment percentage calculations, the AFTAP certification, is either not done or it's done late or it's not clear when it's done.

[Slide 47] Additional issues include assets that are valued differently for Section 430 versus 436. Funding over the IRC 404(o) limitation. This is just the deductible limitation and funding over that and in excess of the deductible limits. And then some notices. Plans are failing to provide the ERISA 101(j) notice timely. In addition, the 204(h) notice for certain plan amendments are not being provided.

Also, ERISA 101(f) requires an annual funding notice. I believe the DOL, the EBSA, has a model notice for the single employer and multi-employer plans you might want to take a look at. And resolution of the qualification failures from these failures have been addressed using the appropriate correction programs and we work with the VCP and Audit CAP agents and apply the basic correction principles.

Let me turn to some common DB cash balance issues.

[Slide 48] Cash balance plans are defined benefit plans that act like defined contribution plans. Cash balance plans are subject to all of the requirements of a defined benefit plan, including the funding requirements of Code Section 430 and the benefit/distribution restrictions of Code Section 436. Schedule SB of Form 5500 filing is required for each year. They are also subject to the participation requirements of Code Section 401(a)(26).

The examinations of the cash balance include some of the issues that are kind of universal to all defined benefit plans, but others also unique to cash balance plans. I mentioned earlier about the late or no AFTAP certifications, and I just want to expound on those a little bit in the cash balance area, although they're no different than the DB in that sense.

So the DB plans, which include cash balance plans, must have their adjusted funding target attainment percentage, the AFTAP, certified by the plan actuary no later than the last day of the ninth month of plan year. For calendar year this is 9/30. If the certification is late, the AFTAP is deemed to fall below 60 percent and the benefit accrual/ distribution restrictions of 436 are imposed. The issue needs to be addressed, and if errors are found, a closing agreement with a potential retroactive amendment may be necessary.

We've seen cases where no AFTAP certification is done and that 60 percent deemed percentage hits and nothing has been done about it, so that's an issue we have to clear up.

Another issue is invalid offsets. Many cash balance plans are offset plans. Revenue Ruling 76-259 provides the rules for a defined benefit plan's benefit to be offset by benefits provided in a defined contribution plan. In the acceptable accrued benefit definition in these offset cash balance plans is: the accrued benefit is set equal to the actuarial equivalent of the projected cash balance account at normal retirement date; offset by the actuarial equivalent of the projected profit-sharing account at normal retirement date.

And the assumptions for each conversion should be defined in the plan. The examinations are finding that a number of plans are offsetting benefits on an annual basis; for example, the plan may have a cash balance credit defined as $50,000 for the owner and half a percent of pay for the non-highly compensated employees. This benefit is then offset by the amount of the profit-sharing plan allocation for the same plan year. This formula does not convert the profit-sharing plan benefit to an annuity when doing the offset, and the conversion to an annuity must take into account the entire profit-sharing account, not just the current year's allocation.

Another area of failure is 401(a)(26) in cash balance plans. We see this often. IRC Section 401(a)(26) requires that a defined benefit plan provide meaningful benefits to at least -- to the lesser -- I'm sorry -- of 40 percent or 50 of the plan sponsor's employees. Plans have been meeting this requirement by defining meaningful benefit for 401(a)(26) purposes as at least a half a percent accrual rate of compensation per year of service.

This definition is causing problems when some cash balance plans are interpreting the half a percent as the annual cash balance credit requirement and forget that the accrual rate in a traditional defined benefit plan refers to an annuity payable at normal retirement date. So if the amount of the cash balance allocation converted to a life annuity by the plan assumption provides for a benefit of less than a half percent of compensation per year of service, that participant may not be receiving a meaningful benefit.

Another area in the cash balance arena, if the plan's definition of a cash balance interest credit ties to the IRC 417(e)(3) rates the applicable interest rate. Prior to PPA, it was acceptable to reference the applicable interest rate as the interest crediting rates - it was the 30-year Treasury rate with the look back month stability period defined. Post PPA, the applicable interest rate is composed of three segment rates which vary depending on when the annuity payments are made.

Some plans adopted the standard model amendment for the applicable interest rate and in operation continue to use the pre-PPA 30-year Treasury rate, or they switched to use one of the segment rates for interest credit, both of which does not follow the plan terms.

Then lastly, another area in the cash balance area is failure with the discrimination under 401(a)(4). And this can happen in many ways, but a couple ways just pointing out that we've seen where the plans have been set up can result from -- those two examples are using short service employees to pass the general test seems to be somewhat prevalent -- or not prevalent, but we find them in some cases. We've run across plans that make use of a very short service employees to pass the discrimination test, and a continual large forfeitures from the profit-sharing plan may suggest this kind of an issue where we would take a look and see who is receiving benefits and whether they meet 401(a)(4).

In addition, using prior service that cannot be included for testing service can be a common misstep in these calculations.

[Slide 49] I want to spend just a few minutes and discuss the Employee Plan Team Audit program. An EPTA audit is a special type of pension plan audit that a team of experienced IRS Employee Plans agents conducts of the plan or plans of a large employer, and EPTA defines large employer as an employer that maintains qualified pension plans that in total have at least 2,500 participants. Agents conduct an in-depth audit of what internal controls an employer has and how the employer applies those controls to a specific plan or plans for a specific open year or years.

[Slide 50] The issues are often similar to other EP examinations; however, the exam will concentrate on process. As these cases include a great deal of data, our computer audit specialist will help us to evaluate and understand how this data is managed and evaluated in terms of the plan.

[Slide 51] Moving to slide 51, some of the common issues on EPTA plans. CAS can check for the required minimum distribution issues, and we are finding them on plans which are frozen and ones that contain legacy benefits. This is both a qualification issue under 401(a)(9) and an excise tax issue as we had previously discussed.

The lost participant issue goes hand-in-hand with the required minimum distribution issue. We have come across situations where no real effort has been made to locate lost participants. There are different things that you can do to show that you have made a good faith effort to locate a lost participant or his beneficiary, but you have to show that you've done it. We also frequently come across compensation issues which result in under or overpayments of benefits to participants. This is a common theme today, I believe. We have also had some issues with cash balance plans, and when we find this issue on examination, we always coordinate with our field actuaries with respect to any required correction.

And finally, we see a lot of non-amenders, late amenders, especially in the case of frozen DB plans. Sometimes I think some plan sponsors believe that once a plan is frozen, they really don't have to do anything other than pay out the remaining assets over time, and this is not correct.

[Slide 52] Finally, I would like to take a moment to talk about some of the multi-employer plan issues, so I want to take a moment to hit on a few of those.

Two of the most common issues with regards to the plan documents are failure to follow provisions contained in the plan, and CBA, the collective bargaining agreement and deficient plan or amendment language. We are continually finding non-collectively bargained employees who are participating in plans without a specific plan section allowing them to participate, or a participation agreement providing for their participation in the plan.

Errors in allocations or contributions in earnings are also happening. Another area is where accruals and service credit are dependent on employer contributions being made to the pension plan, which we should ensure that the crediting of participant accruals and services not dependent on the receipt of related employer contributions.

With the ever-changing environment, funding deficiencies under Section 412 minimum funding requirements, plans are still failing to receive the necessary contributions to satisfy those funding requirements.

The majority of administrators typically rely on participants to apply for benefits before addressing issues. The required minimum distribution requirements of Internal Revenue Code 401(a)(9) are not being met, and we've talked a lot about those, that section and the problems therein.

And finally, a common issue is simply not properly calculating retirement benefits. And these are just some of the errors that we are finding, and I guess I would just go back and say remember, read the plan because so much -- so many of the problems are because of a failure to understand what is in the plan document or misinterpreting the plan document.

So I finished a little bit early. I think we have a few more minutes. So Carol, if you would like, would you like to go back and hit on any of your slides?

Carol Zimmerman:

That sounds like a great idea.

Jeff Milling:

Okay. Then I'll let you conclude it.

Carol Zimmerman:

That sounds fine. That sounds fine.

Jeff Milling:

Okay.

Carol Zimmerman:

[Slide 18] So because we have a few more minutes, let me pick up some of the slides we skipped, and so we'll go back to slide 18. We had talked some about the guidance that was issued on HATFA. The other pension legislation that was passed during 2014 is the CSEC Act for Cooperative and Small Employer Charities. This provides alternative funding rules for certain plans, which are generally those plans with delayed effective dates under Section 104 of PPA '06. There are some exceptions, and I won't spend much time on this because there are only a small number of plans affected, but the changes are significant for those employers. This change -- this legislation created an entire new Code section, Section 433, that's very similar to pre-PPA funding rules, except that there is no deficit reduction contribution. The most important point is that there are several elections that are available regarding effective dates and applicability of these rules. Those elections are due by the end of this year, and we are working on guidance to allow people to know just how to do that and what the implications of those elections would be.

[Slide 19] On slide 19, it's just a reminder that we have issued Notice 2014-19, which deals with the Windsor decision. It was a follow-up to an earlier notice that was issued in 2013, which deals with the Windsor decision that struck down part of DOMA.

Notice 2014-19 says that qualified plans must reflect the Windsor decision effective June 26 of 2013, but the requirement to recognize same-sex marriages based on places celebrated rather than residence is not effective until September 16th, 2013.

Now, earlier application of this Windsor decision is permitted but not required, and there's a fair amount of flexibility. Employers can choose to apply that retroactively for some purposes and not others, but they have to be careful that in doing so, they don't make a decision that would result in a qualification failure, such as something that might affect the nondiscrimination requirements.

Now, many plans don't need amendments because often the definition of "spouse" was not specific about being a man and a woman, but if amendments are needed, they are generally required by 12/31/2014.

[Slide 20] On slide 20 we deal with QLAC regulations. QLACs are Qualified Longevity Annuity Contracts. These contracts allow deeply deferred annuity contracts in retirement accounts, plans with annuities that are starting as late as 85. And these are in defined contribution plans, so like Jeff, I've thrown in one DC bonus here. And the idea of these longevity annuity contracts is that they would provide a safety net to help employees avoid outliving their assets. And the mechanism for doing that is that the required minimum distribution rules would exclude the value of this contract from the account balance, and therefore, you don't run into a situation where you have to make a required minimum distribution but don't have enough cash because too much is locked into the annuity contract.

The final regulations increase the maximum premium that could be put into a qualified longevity annuity contract, and they made other changes that we were told would make them more marketable.

[Slide 21] Slide 21 deals with Revenue Ruling 2014-9 that provides a safe harbor for checking the validity of rollovers to a qualified plan, including DB plans, and generally it means that sponsors can check online to see whether the payor plan was qualified, and the idea is this would make it easier for plan sponsors to accept the rollovers without fear of disqualifying the recipient plan.

[Slide 22] Looking at slide 22, and I know we're getting very close to the time, so we may not be able to cover too much more, but on slide 22, there've been a lot of questions about mortality tables. The current mortality tables were issued in 2007 and then with one year of mortality improvement were reissued in the 2008 regulations. And the Code includes a mandate that we update these tables at least every ten years, so that means we'd have to do it by 2017 or 2018, depending on how you count that. But we do have static mortality tables published for use through 2015 and we intend to stick with those. So you can count on not having new mortality tables until 2016 at the earliest, and it is too early at this point to predict what tables would be issued by the IRS and when. For one, there is a major Society of Actuaries mortality study and they're not expecting to finish their work until October 31, 2014.

And with that, it looks like that's probably as far as we can go without running past our hour, so I think I will stop here and I will thank all of you for attending. We appreciate your attendance, and have a nice day.

Male Voice:

Thank you very much. This does conclude today's teleconference. We thank you for your participation. You may disconnect your lines at this time, and have a great day.